



**SECURITIES AND EXCHANGE COMMISSION**  
**[Release No. 34-96415; File No. SR-FINRA-2022-031]**

**Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Adopt FINRA Rules 6151 (Disclosure of Order Routing Information for NMS Securities) and 6470 (Disclosure of Order Routing Information for OTC Equity Securities)**

November 30, 2022.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on November 16, 2022, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

**I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change**

FINRA is proposing to adopt FINRA Rules 6151 (Disclosure of Order Routing Information for NMS Securities) and 6470 (Disclosure of Order Routing Information for OTC Equity Securities) to require members to (i) publish order routing reports for orders in OTC Equity Securities, and (ii) submit their order routing reports for both OTC Equity Securities and NMS Securities to FINRA for publication on the FINRA website.

The text of the proposed rule change is available on FINRA’s website at <http://www.finra.org>, at the principal office of FINRA and at the Commission’s Public Reference Room.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Rule 606(a) of Regulation NMS<sup>3</sup> (“SEC Rule 606(a)”) requires broker-dealers to publicly disclose specified information about their order routing practices for NMS Securities,<sup>4</sup> including for non-directed orders in NMS stocks that are submitted on a “held” basis.<sup>5</sup> The SEC has stated that, as a result of these disclosures, “customers—and retail investors in particular—that submit orders to their broker-dealers should be better able to assess the quality of order handling services provided by their broker-dealers and whether their broker-dealers are effectively managing potential conflicts of interest.”<sup>6</sup>

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<sup>3</sup> 17 CFR 242.606(a).

<sup>4</sup> Generally, “NMS Securities” include listed stocks and options, and NMS stocks means any NMS Security other than an option. See 17 CFR 242.600(b).

<sup>5</sup> See Securities Exchange Act Release No. 84528 (November 2, 2018), 83 FR 58338 (November 19, 2018) (Disclosure of Order Handling Information; Final Rule) (“2018 Amendments Release”). The SEC did not specifically define “held” or “not held” orders, but stated that typically a “not held” order provides the broker-dealer with price and time discretion in handling the order, whereas a broker-dealer must attempt to execute a “held” order immediately. See id. at 58340 n.19. As noted by the SEC in the 2018 Amendments Release, broker-dealers utilize the “held” and “not held” order classifications as a matter of industry practice and to comply with regulatory requirements, including audit trail reporting requirements and the definition of “covered order” in Rule 600(b) of Regulation NMS. See id. at 58344.

<sup>6</sup> See 2018 Amendments Release, 83 FR 58338, 58423.

FINRA believes these same goals would be furthered by providing investors with similar order handling information for unlisted stocks, which are not covered by the existing SEC Rule 606(a) disclosure requirements.<sup>7</sup> Accordingly, FINRA is proposing to adopt new Rule 6470 to require members to publish quarterly order routing disclosures primarily for non-directed held orders in OTC Equity Securities,<sup>8</sup> generally aligned with the SEC Rule 606(a) disclosures for NMS stocks but with modifications to account for differences between the market for NMS Securities and over-the-counter (“OTC”) markets, as described below. In addition, to make both the existing SEC Rule 606(a) disclosures and the new OTC Equity Security disclosures more accessible to investors, FINRA is proposing new Rule 6151 and paragraph (d) of new Rule 6470 to require members to send both disclosures to FINRA for centralized publication on the FINRA website, as described further below.

#### Disclosure of Order Routing Information for OTC Equity Securities

Proposed new Rule 6470, entitled “Disclosure of Order Routing Information for OTC Equity Securities,” would require the publication of order routing disclosures for OTC Equity Securities. Specifically, as is already required for broker-dealers with respect to held orders in NMS stocks under SEC Rule 606(a)(1), proposed Rule 6470(a) would require, among other things, every member to make publicly available for each calendar quarter a report on its routing of non-directed orders in OTC Equity Securities that are submitted on a held basis during that quarter, broken down by calendar month, and keep such report posted on an internet website that is free and readily accessible to the public for a period of three years from the initial date of

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<sup>7</sup> FINRA notes that the SEC’s Equity Market Structure Advisory Committee (“EMSAC”) previously recommended enhancing the current order routing disclosures required under SEC Rule 606 with information about OTC Equity Securities, and also expressed support for centralization of the reports. See EMSAC, Recommendations Regarding Modifying Rule 605 and Rule 606 (November 29, 2016), <https://www.sec.gov/spotlight/emsac/emsac-recommendations-rules-605-606.pdf>.

<sup>8</sup> An “OTC Equity Security” means any equity security that is not an NMS stock, other than a Restricted Equity Security. See FINRA Rule 6420(f). A “Restricted Equity Security” means any equity security that meets the definition of “restricted security” as contained in Securities Act Rule 144(a)(3). See FINRA Rule 6420(k).

posting on the internet website.<sup>9</sup> Also in line with the required publication timeframe for NMS stock disclosures under SEC Rule 606(a)(2), proposed Rule 6470(c) would require that a member make the new OTC Equity Security report publicly available within one month after the end of the quarter addressed in the report.<sup>10</sup>

Under Rule 606(a)(1), the SEC Rule 606(a) reports for NMS Securities are required to be broken out into separate sections for NMS stocks in the S&P 500 Index as of the first day of the quarter, other NMS stocks, and NMS Securities that are options. Since these categories are not relevant to the OTC market, FINRA is proposing to instead require that the new quarterly reports for OTC Equity Securities under Rule 6470(a) be separated into three sections to better reflect the OTC market. Specifically, the new reports would be required to be separated into three sections for: (i) domestic OTC Equity Securities; (ii) American Depositary Receipts (“ADRs”) and foreign ordinaries that are OTC Equity Securities; and (iii) Canadian-listed securities trading

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<sup>9</sup> Proposed Rule 6470 would apply to “every member,” but FINRA notes that the focus of the proposed disclosures is held orders from customers in OTC Equity Securities, and some members may not engage in any activities involving held orders from customers in OTC Equity Securities. If a member does not accept any orders in OTC Equity Securities from customers during a given calendar quarter (whether held or not held), such member would not be required to publish a report under Rule 6470 for that quarter. Similarly, a member that accepted only not held orders in OTC Equity Securities from customers—but no held orders in OTC Equity Securities from customers—during a given calendar quarter would not be required to publish a report for that quarter. See infra note 21. Further, if a member accepted orders in OTC Equity Securities (whether held, not held, or both) only from other broker-dealers, but not from customers, during a given calendar quarter, such member would not be required to publish a report for that quarter.

<sup>10</sup> FINRA understands that some introducing firms route all of their orders in OTC Equity Securities to one or more clearing firms for further routing to other venues for execution. The SEC has provided guidance that, where an introducing firm routes all of its covered orders to one or more clearing firms for further routing and execution and the clearing firm in fact makes the routing decision, the introducing firm generally may comply with the order routing disclosure requirements by: (i) disclosing its relationship with the clearing firm(s) on its website that includes any payment for order flow received by the introducing firm, and (ii) adopting the clearing firm’s disclosures by reference, provided that the introducing firm has examined the report and does not have reason to believe it materially misrepresents the order routing practices. FINRA intends to provide parallel guidance with respect to proposed Rule 6470. See SEC Division of Trading and Markets, Responses to Frequently Asked Questions Concerning Rule 606 of Regulation NMS, Question 12.01; see also SEC Division of Market Regulation, Staff Legal Bulletin No. 13A, Frequently Asked Questions About Rule 11Ac1-6, Question 4.

in the United States as OTC Equity Securities. To provide for consistency across member reports, FINRA will publish a list of the OTC Equity Security symbols that fall under each category, and members would be required to publish reports in a manner consistent with such list.<sup>11</sup>

Under Rule 606(a)(1), the SEC Rule 606(a) reports for NMS Securities must be made available using the most recent versions of the XML schema and associated PDF renderer as published on the SEC's website. Similarly, Rule 6470(a) would specify that the new OTC Equity Security reports must be made available using the most recent versions of the XML schema and associated PDF renderer as published on the FINRA website. FINRA believes this requirement would ensure that reports are generated and published in standardized machine-readable and human-readable forms, which would benefit investors by permitting the public to more easily analyze and compare the OTC Equity Security reports across members, as well as to more easily perform combined analysis of both SEC Rule 606(a) and OTC Equity Security reports.<sup>12</sup>

With respect to the content of the new reports, Rule 6470(a) would require that each section of the new OTC Equity Security reports include the information specified in paragraphs (a)(1) through (4) of proposed Rule 6470, specifically:<sup>13</sup>

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<sup>11</sup> If the Commission approves the proposed rule change, FINRA will provide information in the Regulatory Notice announcing the effective date regarding where members may access the list of OTC Equity Security symbols that FINRA will maintain on its website.

<sup>12</sup> FINRA would publish the technical specifications for the XML schema and associated PDF renderer on its website for member use in generating the new reports. FINRA expects that, subject to the differences between the SEC Rule 606(a) reports and the OTC Equity Security reports discussed above, the XML schema and associated PDF renderer published by FINRA would be substantially similar to those published by the SEC for the SEC Rule 606(a) reports.

<sup>13</sup> A template of the proposed new OTC Equity Security report that would be required under proposed Rule 6470 is attached as Exhibit 3 [sic].

- the percentage of total orders<sup>14</sup> for the section that were not held orders and held orders, and the percentage of held orders for the section that were non-directed orders;<sup>15</sup>
- the identity of the ten venues to which the largest number of total non-directed held orders for the section were routed for execution<sup>16</sup> and of any venue to which five percent or more of non-directed held orders for the section were routed for execution, and the percentage of total non-directed held orders for the section routed to the venue;<sup>17</sup>

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<sup>14</sup> For purposes of proposed Rule 6470(a), “total orders” would include all orders from customers for the section, including both directed and non-directed orders from customers.

<sup>15</sup> For purposes of the proposed disclosures, a “non-directed order” would mean any order from a customer other than a directed order. Consistent with the definition of “directed order” under Regulation NMS, a “directed order” would mean an order from a customer that the customer specifically instructed the member to route to a particular venue for execution. See 17 CFR 242.600(b); see also 2018 Amendments Release, 83 FR 58338, 58339 n.4. FINRA notes that, similar to the definition of “customer” under Rule 600(b)(23) of Regulation NMS, a “customer” is defined under FINRA rules to exclude a broker or dealer. See FINRA Rule 0160(b)(4). Orders from other broker-dealers would therefore be excluded from the proposed disclosures.

<sup>16</sup> Consistent with the SEC’s approach to SEC Rule 606(a), FINRA intends that, for purposes of the proposed disclosures for OTC Equity Securities, a “venue” would be defined broadly to cover any market center or any other person or entity to which a member routes orders for execution. See, e.g., Securities Exchange Act Release No. 43590 (November 17, 2000), 65 FR 75414, 75427 n.63 (December 1, 2000) (Disclosure of Order Execution and Routing Practices) (“The term ‘venue’ is intended to be interpreted broadly to cover ‘market centers’ within the meaning of Rule 11Ac1–5(a)(14) [now Rule 600(b)(46) of Regulation NMS], as well as any other person or entity to which a broker routes non-directed orders for execution. Consequently, the term excludes an entity that is used merely as a vehicle to route an order to a venue selected by the broker-dealer.”); see also 17 CFR 242.600(b)(46) (“Market center means any exchange market maker, OTC market maker, alternative trading system, national securities exchange, or national securities association.”). Accordingly, for purposes of proposed Rule 6470, where an alternative trading system (“ATS”) offers both automatic order execution and order delivery functionality, the ATS should be identified as the venue only when the ATS provides order execution. FINRA believes identification of the ATS in these circumstances is appropriate because the ATS is the venue where the order was routed “for execution,” consistent with SEC guidance for the predecessor to SEC Rule 606. See SEC Division of Market Regulation, Staff Legal Bulletin No. 13A, Frequently Asked Questions About Rule 11Ac1-6, Question 12. Conversely, for purposes of proposed Rule 6470, in cases where the ATS instead provides order delivery, the separate market center to which the orders are delivered—e.g., a market maker or other ATS—should be identified as the venue where the order was routed for execution.

<sup>17</sup> However, the proposed rule change would include a de minimis venue exception parallel to exemptive relief that the SEC has provided with respect to the SEC Rule 606(a)

- for each identified venue, the net aggregate amount of any payment for order flow received, payment from any profit-sharing relationship received, transaction fees paid, and transaction rebates received, both as a total dollar amount and per order, for all non-directed held orders for the section; and
- a discussion of the material aspects of the member's relationship with each identified venue, including, without limitation, a description of any arrangement for payment for order flow and any profit-sharing relationship and a description of any terms of such arrangements, written or oral, that may influence a member's order routing decision including, among other things: incentives for equaling or exceeding an agreed upon order flow volume threshold, such as additional payments or a higher rate of payment; disincentives for failing to meet an agreed upon minimum order flow threshold, such as lower payments or the requirement to pay a fee; volume-based tiered payment schedules; and agreements regarding the minimum amount of order flow that the member would send to a venue.<sup>18</sup>

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reports. See Letter from Annette L. Nazareth, Director, SEC Division of Market Regulation, to Neal E. Sullivan & Gail Marshall-Smith, Bingham Dana LLP (on behalf of First Union Securities, Inc.), dated June 22, 2001, 2001 SEC No-Act. LEXIS 903; see also SEC Division of Market Regulation, Staff Legal Bulletin No. 13A, Frequently Asked Questions About Rule 11Ac1-6, Question 2. Specifically, proposed Rule 6470(b) would provide an exception from the requirement for a member to identify venues that received less than 5% of non-directed held orders for a section, provided that the member has identified the top execution venues that in the aggregate received at least 90% of the member's total non-directed held orders for the section.

<sup>18</sup> Similar to SEC Rule 606(a), the types of arrangements referenced above are not an exhaustive list of terms of payment for order flow arrangements or profit-sharing relationships that may influence a broker-dealer's order routing decision that would be required to be disclosed. For example, if a broker-dealer receives a discount on executions in other securities or some other advantage in directing order flow in a specific security to a venue, or if a broker-dealer receives equity rights in a venue in exchange for directing order flow there, then all terms of those arrangements would also be required to be disclosed. Similarly, if a broker-dealer receives variable payments or discounts based on order types and the number of orders sent to a venue, such arrangements would be required to be disclosed. See 2018 Amendments Release, 83 FR 58338, 58376 n.397. However, FINRA notes that these are only examples, and a member would be required to disclose any other material aspects of its relationship with

The proposed content of the new OTC Equity Security reports under proposed FINRA Rule 6470(a) generally parallels the content required to be included in SEC Rule 606(a) reports for NMS stocks pursuant to SEC Rule 606(a)(1)(i) through (iv), with the following differences to take into account the different market structure and characteristics of OTC Equity Securities. First, Rule 6470(a)(1) would require members to disclose the percentage of total orders for the section that were not held orders and held orders, in addition to disclosing the percentage of held orders for the section that were non-directed orders.<sup>19</sup> While SEC Rule 606(a) similarly requires broker-dealers to disclose the percentage of orders for each section that were non-directed orders, it does not require broker-dealers to disclose the percentage of total orders for each section that were not held orders and held orders.<sup>20</sup> FINRA believes that requiring members to provide information about the relative amount of a member's held and not held orders in the new reports proposed to be published under Rule 6470(a)(1) would provide investors, regulators, academics, and others seeking to review the reports with additional information regarding the business of brokers active in the OTC market.<sup>21</sup>

Second, the information required to be disclosed under SEC Rule 606(a)(i) through (iii) is required to be broken out into sections for market orders, marketable limit orders, non-marketable limit orders, and other orders. However, FINRA is not adopting these categories for

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each identified venue regardless of whether a particular example is listed in the proposed rule text or otherwise discussed in this proposed rule change.

<sup>19</sup> See notes 14 and 15 *supra*.

<sup>20</sup> SEC Rule 606(b)(1) provides that customers may request customer-specific information about the handling of both their held and not held orders, and SEC Rule 606(b)(3) provides that customers may request additional customer-specific information about the handling of their not held orders. FINRA is not proposing parallel customer-specific disclosure requirements for OTC Equity Securities at this time.

<sup>21</sup> The proposed requirement to disclose the percentage of total orders for each section that were not held orders and held orders is the only disclosure requiring any information regarding not held orders, as the remainder of the proposed disclosures apply exclusively to held orders. If a member did not accept any held orders in OTC Equity Securities from customers in a given calendar quarter, it would not be required to publish a report under proposed Rule 6470 for that quarter (even if it accepted orders on a not held basis during that quarter). See note 9, *supra*.



OTC Equity Securities due to the absence of a centralized, self-regulatory organization (SRO)-disseminated national best bid and offer in the OTC market on which to standardize and base marketability. Finally, SEC Rule 606(a)(1)(iii) requires the disclosure of quantitative payment information both as a total dollar amount and per share. In light of different pricing practices in the OTC market, Rule 6470(a)(3) would instead require the quantitative disclosures for OTC Equity Securities to be expressed as both a total dollar amount and per order (rather than per share).<sup>22</sup>

#### Centralized Hosting of Order Routing Disclosures

As discussed above, SEC Rule 606(a) requires broker-dealers to publish their SEC Rule 606(a) reports for NMS Securities on an internet website that is free and readily accessible for at least three years, and proposed FINRA Rule 6470 would similarly require the new OTC Equity Security reports to be published on a website that is free and readily accessible for at least three years. Currently there is not one location where all SEC Rule 606(a) reports are consolidated, although FINRA understands some broker-dealers use vendors that make their client broker-dealers' reports available through common vendor pages. Thus, regulators, investors and others seeking to review the reports often must locate and obtain the reports from various individual broker-dealer or vendor websites.

To make both the existing Rule 606(a) reports and the new OTC Equity Security reports more accessible for regulators, investors and others seeking to analyze and compare the data, FINRA is proposing to require that members provide the reports to FINRA for central publication on the FINRA website (in addition to posting on a public website for at least three years, as required under Rule 606(a) and proposed Rule 6470(a)).<sup>23</sup> Specifically, paragraph (d)

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<sup>22</sup> For example, FINRA understands that, unlike in the market for NMS Securities where payment for order flow is typically paid as a specified dollar amount per share, payments in the OTC market are predominantly made on a per order basis (with rates typically bucketed by share price category).

<sup>23</sup> FINRA also intends to engage in investor education efforts to help investors and others understand the purpose, content, and potential limitations of the disclosures.

of proposed new Rule 6470 would require each member to provide the OTC Equity Security report to FINRA within one month after the end of the quarter addressed in the report in such a manner as may be prescribed by FINRA.<sup>24</sup> Proposed new Rule 6151, entitled “Disclosure of Order Routing Information for NMS Securities,” would similarly require each member that is required to publish a report pursuant to SEC Rule 606(a) to provide the report to FINRA, in the manner prescribed by FINRA, within the same time and in the same formats that such report is required to be made publicly available pursuant to SEC Rule 606(a) (*i.e.*, one month after the end of the calendar month addressed in the report). Under both provisions, FINRA would publish such reports on its public website. FINRA will publish both the SEC Rule 606(a) and OTC Equity Security reports in a centralized location on the FINRA website, free of charge and with no restrictions on use of the data.<sup>25</sup>

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<sup>24</sup> FINRA would specify details regarding the manner of submission of the reports to FINRA in a Regulatory Notice or similar publication. Members would be permitted to use a third-party vendor to assist with both the generation of the reports and transmission to FINRA. However, the member would remain responsible for the reports in all respects, including the accuracy of the disclosures and the timeliness and completeness of the submissions to FINRA. Accordingly, a member would be required to submit a corrected report to FINRA (and publish a corrected report on its publicly accessible website) promptly following the discovery of inaccurate data or other error in a previously submitted or posted report.

<sup>25</sup> As noted above, the SEC has provided guidance that introducing firms may comply with Rule 606(a) by incorporating their clearing firm(s) reports in specified circumstances, and FINRA intends to provide similar guidance with respect to the OTC Equity Security reports required under proposed Rule 6470. See supra note 10. To facilitate centralized access to the reports, such introducing firms must provide FINRA with a list of their clearing firm(s) and the hyperlink to the webpage where they disclose their clearing firm relationship(s) and adopt the clearing firm(s)’s reports by reference. Each introducing firm relying on this guidance would be required to provide this information to FINRA upon implementation of the proposed rule change and to update FINRA if the information previously provided changes. This information will enable FINRA to provide investors with relevant information for all firms, including introducing firms incorporating clearing firm reports by reference, on FINRA’s website.

If the Commission approves the proposed rule change, FINRA will announce the effective date of the proposed rule change in a Regulatory Notice. The effective date will be no later than 365 days following publication of the Regulatory Notice announcing Commission approval of the proposed rule change.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>26</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

FINRA believes that the proposed requirement for members to publish order routing disclosures for OTC Equity Securities, similar to what is available under SEC rules for NMS Securities, would provide valuable information for investors and other market participants, academics, regulators and others regarding order routing practices in the OTC market, thereby enhancing the protection of investors and the public interest. In particular, these new disclosures will enable investors to better assess the quality of their broker-dealers' order handling services for these securities, provide more information on the financial incentives that may affect their broker-dealers' routing decisions, and allow investors to better evaluate whether their broker-dealers are effectively managing potential conflicts of interest. The proposed requirements for members to send their disclosure reports for both NMS Securities and OTC Equity Securities to FINRA for centralized publication on the FINRA website will make this important information more accessible for regulators, investors, academics and others seeking to analyze and compare the data, particularly across firms, and would facilitate the ability of FINRA and the SEC to review the data for regulatory purposes.

## B. Self-Regulatory Organization's Statement on Burden on Competition

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<sup>26</sup> 15 U.S.C. 78o-3(b)(6).

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

#### Economic Impact Assessment

Based on the regulatory need discussed above and summarized below, FINRA has undertaken an economic impact assessment, as set forth below, to analyze the potential economic impacts of the proposed rule change, including potential costs, benefits, and distributional and competitive effects, relative to the current baseline.

#### Regulatory Need

FINRA believes that in today's markets, where various incentives may impact broker-dealers' order handling decisions, customers have limited access to relevant information to help them assess how their orders are handled, and that different customers may have access to different amounts or categories of relevant information. The proposed requirement for members to publish quarterly order routing disclosures for non-directed held orders in OTC Equity Securities is designed to provide investors with information to better assess the quality of order handling services provided by their broker-dealers and whether their broker-dealers are effectively managing potential conflicts of interest. In addition, requiring members to send both the existing SEC Rule 606(a) disclosures and the proposed OTC Equity Security disclosures to FINRA for centralized publication on the FINRA website would make these disclosures more accessible to investors and others relevant stakeholders.

#### Economic Baseline

Between October 1 and December 31, 2020, there were 85, 76, and 55 firms<sup>27</sup> quoting domestic OTC Equity Securities, ADRs and foreign ordinaries that are OTC Equity Securities, and Canadian-listed securities trading in the U.S. as OTC Equity Securities, respectively. The average number of symbols quoted per firm in each of these respective security categories was:

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<sup>27</sup> A "firm" is any FINRA member that has a Central Registration Depository number.

496, 681, and 260. Furthermore, the average number of quote events per symbol and firm, 37,831, was the largest for Canadian-listed securities that trade OTC in the U.S. as compared to 1,203 for domestic and 25,105 for ADRs and foreign ordinaries.

There are more firms executing trades than providing quotes in OTC Equity Securities. In the fourth quarter of 2020, there were 261, 250, and 196 firms executing trades in domestic, ADRs and foreign ordinaries, and Canadian-listed securities trading in the U.S. as OTC Equity Securities, respectively. The average number of symbols traded per firm was 287, 491, and 195, and the average number of executions per symbol and per firm was 1,215, 1,082, and 1,381 for these respective security categories. Although the average number of executions per symbol per firm was largest for Canadian-listed securities, the average dollar volume per symbol and per firm was largest for the ADRs and foreign ordinaries at \$7,687,626, as compared to \$3,621,871 for domestic and \$2,660,868 for the Canadian-listed securities that trade OTC in the U.S. This reflects the generally lower prices for domestic OTC Equity Securities and Canadian-listed securities that trade OTC in the U.S. as compared to ADRs and foreign ordinary shares.

In the fourth quarter of 2020, there were 560, 573, and 444 firms that routed orders in domestic OTC Equity Securities, ADRs or foreign ordinaries, and Canadian-listed securities that trade as OTC Securities in the U.S, respectively, with approximately 600 unique firms total across the three categories. These numbers represent the potential upper bound on the number of firms by security category that could be required to provide the proposed disclosure reports, as some firms may not handle orders from customers (based on fourth quarter of 2020 data). The average number of symbols routed per firm is 104, 180, and 67, and the average number of orders per symbol and per firm is 170, 124, and 134 for each of the three security categories. Consequently, the largest average number of symbols routed per firm was for ADRs and foreign ordinaries, but the average number of orders per symbol per firm was largest for domestic OTC Equity Securities.

FINRA believes that, at present, customers receive limited information on how members

route their orders in OTC Equity Securities, any payments that members receive from execution venues related to the routing of these orders, and the relative order execution quality by member or execution venue. In the absence of regulatory disclosure requirements, any information that customers do receive may be selectively provided to individual customers and is likely not comparable across firms. Moreover, larger customers may receive more information relative to smaller customers, thereby giving the former an informational advantage. OTC Equity Security routing data is currently not required to be publicly available, and no studies have been conducted on the quality of order handling services provided by firms for such securities.

There are, however, studies that examine the benefits of transparency around the implementation of Rules 605<sup>28</sup> and 606 of Regulation NMS with respect to member routing and venue execution quality for NMS stocks. These studies may inform the potential economic impacts from transparency in the market for OTC Equity Securities, although, as noted above, there are significant differences between the market for NMS Securities and OTC Equity Securities. In addition, as Rules 605 and 606 went into effect at approximately the same time, these studies are unable to distinguish the separate effects of order execution quality disclosure under Rule 605 and that of order routing disclosure under Rule 606 on activity in NMS stocks. After implementation of Rule 605, effective and quoted spreads for NYSE-, AMEX-, and NASDAQ-listed stocks declined significantly.<sup>29</sup> In addition, the implementation of Rules 605 and 606 resulted in broker-dealers increasingly routing orders in NMS stocks to venues that offered better execution quality on the dimensions of effective spreads and fill rates, which

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<sup>28</sup> Under Rule 605 (formerly 11Ac1-5), the SEC requires market centers that trade NMS Securities to make monthly electronic reports. These reports include information about each market center's quality of executions on a stock-by-stock basis, including how market orders of different sizes are executed relative to the public quotes. These reports also disclose information about effective spreads and the extent to which executions occur at prices better than the public quotes for marketable orders.

<sup>29</sup> See Xin Zhao & Kee H. Chung, Information Disclosure and Market Quality: The Effect of SEC Rule 605 on Trading Costs, 42 The Journal of Financial and Quantitative Analysis, 657-682 (2007).

suggests these reports contain information that appears useful in routing decisions.<sup>30</sup>

Studies analyzing the market for NMS stocks indicate that broker-dealers may route orders to maximize order flow payments by sending market orders to venues making payments and sending limit orders to venues paying large liquidity rebates. Such routing may not always be in customers' best interests. Make-take fees may lead to agency conflicts and rebate volume pricing tiers may worsen such conflicts further.<sup>31</sup> Theoretical models of the conflict between investors and their broker-dealers, who may be incentivized to route orders based on the take fees charged or rebates paid by exchanges, find that the conflict of interest reduces investor utility.<sup>32</sup> Using Rule 606 data, one study examined broker-dealer routing of non-marketable limit orders in NMS stocks to exchanges offering the largest rebate. This analysis combined with proprietary limit order data found that low-fee (*i.e.*, low-rebate) exchanges fill or fill more rapidly when high-fee (*i.e.*, high-rebate) exchanges do not fill, and non-marketable limit orders earn higher average realized spreads on low-fee than high-fee exchanges.<sup>33</sup>

In the absence of the proposed disclosures, investors may not know where a broker-dealer routes orders for execution or whether the broker-dealer receives payments or rebates from such venues. In addition, in the absence of order routing and payment for order flow information, customers may not possess information necessary to assist them in forming a preference concerning their brokers' routing choices—particularly where customer commission charges have been reduced or eliminated. Furthermore, if customers have information on how

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<sup>30</sup> See Ekkehart Boehmer, Robert Jennings, & Li Wei, Public Disclosure and Private Decisions: Equity Market Execution Quality and Order Routing, 20 Review of Financial Studies, 315–358 (2007).

<sup>31</sup> See James J. Angel, Lawrence E. Harris & Chester S. Spatt, Equity Trading in the 21st Century,” 1 Quarterly Journal of Finance, 1–53 (2011); Chester S. Spatt, Is Equity Market Exchange Structure Anti-Competitive? (Dec. 28, 2020) Working Paper.

<sup>32</sup> See David A. Cimon, Broker Routing Decisions in Limit Order Markets, 54 Journal of Financial Markets, 1386-4181 (2021).

<sup>33</sup> See Robert Battalio, Shawn A. Corwin & Robert Jennings, Can Brokers Have It All? On the Relation Between Make-Take Fees and Limit Order Execution Quality, 71 The Journal of Finance, 2193–2238 (2016).

brokers route orders and are able to negotiate commissions to more closely represent the broker-dealer's average execution cost for a particular customer's order flow, then customers may be better able to submit the mix of liquidity-supplying and demanding orders to minimize commissions and improve order execution.<sup>34</sup> Even where customers are unable to negotiate fees, agency issues related to order flow payments may be reduced or eliminated if investors know where their orders are routed. As noted above, while these studies examine the benefits of transparency with respect to NMS stocks and there are significant differences between the market for NMS Securities and the market for OTC Equity Securities, these studies may inform analysis of the potential impacts of the proposed disclosure on the OTC market.

### Economic Impacts

#### Anticipated Benefits

Under the proposed rule change, customers would have more information on the financial incentives that may affect their firms' routing decisions, because the reports would identify the net aggregate amount of any payment for order flow received, payment from any profit-sharing relationship received, transaction fees paid, and transaction rebates received by their firms.

At present, in the absence of order routing reports, customers may be less able to consider indirect costs that may impact execution quality than direct trading costs, such as commissions charged. This is particularly true for retail investors that use the services of zero-commission broker-dealers. Under the proposed rule change, customers may more easily consider indirect and less observable costs, such as transaction fees paid less rebates or payment for order flow, and better assess potential conflicts of interest. Brokerage commissions, if charged, may depend on the amount of payment for order flow received and net make-take fees paid by the firm. For example, members that earn more payment for order flow may pass a portion of this revenue on to customers by offering lower commissions. However, routing solely to maximize rebates or

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<sup>34</sup> See Shawn M. O'Donoghue, Transaction Fees: Impact on Institutional Order Types, Commissions, and Execution Quality, 60 Journal of Financial Markets (2022).



minimize transaction fees may result in lower execution quality than alternative routing strategies and may raise best execution concerns. Without the proposed disclosures, customers may primarily assess the amount of commissions, if charged, when evaluating brokerage service costs. Customers may pay higher net trading costs should zero or lower commission firms offer inferior execution quality. Standardized reports, which would be available on the member's website and centralized on FINRA's website, would allow customers to compare order routing practices across different firms and observe changes in a firm's routing behavior over time. Customers would be able to better compare indirect trading costs and whether payment for order flow received and net transaction fees paid, considering rebates, may be affecting the routing decisions of some firms more than others or causing changes in routing behavior over time. The information in these reports would permit customers to evaluate firms' routing decisions more effectively and be better informed in making choices among firms. Dividing OTC Equity Securities into separate sections depending on whether they are domestic, ADRs or foreign ordinaries, or Canadian-listed OTC Equity Securities would provide customers with meaningful categories and potentially make the information more useful than if all securities were presented in one group.

FINRA believes that direct benefits to customers stemming from the proposed standardized reports may be limited by a customer's ability to interpret the information in the reports or compare the reports across different members or over time. However, customers may also benefit indirectly through changes in a firm's behavior. A firm may use the standardized reports to compare its order routing to that of competing firms, and subsequently, to improve its order execution quality. Thus, firms that do not route solely based on payment for order flow received, net transaction fees paid (inclusive of rebates), or provide relatively better order execution quality may better compete for customers based on not receiving rebates or providing

better order execution quality.<sup>35</sup> In addition, academic or industry researchers may analyze the data in the proposed public reports, which will be centralized on FINRA's website, and make their findings describing differences in broker-dealer routing practices public.

Because FINRA members would be required to submit their existing Rule 606(a) reports to FINRA for central publication on the FINRA website, investors and academic and other industry researchers may more easily access the SEC Rule 606(a) reports, which should make it easier for users to examine data in SEC Rule 606(a) reports across broker-dealers. The reporting and centralization of both the new OTC Equity Security reports and the existing Rule 606(a) reports should also ease FINRA's access to the reported data for regulatory purposes, thereby reducing FINRA's costs.

#### Anticipated Costs

Members may incur fixed costs, such as programming, to create the initial proposed reports. These initial costs may vary depending on whether firms collect the data and produce the reports in-house or outsource the process to a third party. Members may pay costs to identify which orders are non-directed and submitted on a held basis and determine the net aggregate amount of any payment for order flow received and net rebates received in total and per order. To the extent that a member already has systems in place to create reports required for NMS Securities under Rule 606(a), which is probable in most cases, then these initial fixed costs may be relatively lower for such members, although the extent to which these costs would be lower for such firms would depend on the degree to which their existing systems for NMS Securities' disclosures may be used for OTC Equity Securities. Once the system to create the proposed reports is built, there would be fixed costs for maintaining the system and on-going compliance costs, and variable costs for creating and posting the publicly available quarterly reports and for

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<sup>35</sup> In light of differences between the market for NMS Securities and the market for OTC Equity Securities, including for example the absence of a centralized, SRO-disseminated national best bid and offer in the OTC market, FINRA is not proposing execution quality disclosure requirements for OTC Equity Securities at this time.

transmitting the reports to FINRA.

In addition, firms that route orders in OTC Equity Securities may re-evaluate their best execution evaluation methodologies and, if deemed beneficial, may choose to incorporate information from the proposed publicly available reports posted by competing firms, which may or may not involve costs to the firm depending on how a firm chooses to use this information.<sup>36</sup> Furthermore, as noted by the Commission with respect to new disclosure requirements under Rule 606(b)(3), “[g]iven that broker-dealers will be aware of the metrics to be used a priori, they might route not held orders in a manner that promotes a positive reflection on their respective services but that may be suboptimal for their customers.”<sup>37</sup> FINRA notes the same possibility in connection with the proposed rule change requiring the disclosure of OTC order handling disclosures. However, FINRA also notes any such effects would be constrained by a firm’s obligations under FINRA Rule 5310. In addition, to the extent that the proposal increases costs to members, particularly smaller firms, they may attempt to recoup costs by increasing fees for customers or modifying the scope of services offered for OTC Equity Securities.

Further, if firms stop or limit routing orders to venues paying rebates or making payments for order flow given the existence of the proposed reports, then these venues may reduce or eliminate these financial incentives as volumes decline, which could in turn impact the extent to which a market participant is willing to provide liquidity at such venues, potentially resulting in fewer quotes, wider bid-ask spreads, or fewer shares posted at such venues. In addition, the cost of capital for firms that issue OTC Equity Securities may increase if their securities become less liquid. Because members will be responsible for submitting SEC Rule 606(a) reports currently required for NMS Securities under Regulation NMS to FINRA, they will bear either a direct cost

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<sup>36</sup> While firms that route orders in OTC Equity Securities may re-evaluate their best execution evaluation methodologies and incorporate information from the proposed reports, the proposed new OTC Equity Security order routing disclosure reports themselves would not alter a firm’s best execution obligations.

<sup>37</sup> See 2018 Amendments Release, 83 FR 58338, 58425.

to send the reports to FINRA or an indirect cost if an agent sends the report on their behalf. FINRA believes that introducing firm members that choose to rely on the proposed guidance<sup>38</sup> would incur lower costs compared to preparing and providing the actual reports on a quarterly basis on their own or through a third-party vendor.

#### Alternatives Considered

No other alternatives were considered for the proposed amendments.

#### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The proposed rule change was published for comment in Regulatory Notice 21-35 (October 2021). Five comments were received in response to the Regulatory Notice.<sup>39</sup> A copy of the Regulatory Notice is available on FINRA's website at <http://www.finra.org>. Copies of the comment letters received in response to the Regulatory Notice are also available on FINRA's website. The comments are summarized below.

NASAA supported the proposed rule change, stating that it is appropriately tailored to reveal potential conflicts of interest and would bring additional transparency to trading practices in the OTC market.<sup>40</sup> NASAA also expressed support for FINRA's publication of order routing reports on its website, noting that centralization of the reports would allow investors to make comparisons easily, help inform and facilitate regulatory decisions, and help FINRA analyze

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<sup>38</sup> See supra notes 10 and 25.

<sup>39</sup> See Comment submission from Keith L Hickman, dated October 7, 2021; letter from Howard Meyerson, Managing Director, Financial Information Forum, to Jennifer Piorko Mitchell, Office of the Corporate Secretary, FINRA, dated December 2, 2021 ("FIF Letter"); letter from Derrick Chan, Head of Equity Trading and Sales, Fidelity Investments, to Jennifer Piorko Mitchell, Office of the Corporate Secretary, FINRA, dated December 6, 2021 ("Fidelity Letter"); letter from Michelle Bryan Oroschakoff, Chief Legal Officer, LPL Financial, to Jennifer Piorko Mitchell, Office of the Corporate Secretary, FINRA, dated December 6, 2021 ("LPL Letter"); and letter from Melanie Senter Lubin, President, North American Securities Administrators Association, Inc., to Jennifer Piorko Mitchell, Office of the Corporate Secretary, FINRA, dated December 6, 2021 ("NASAA Letter").

<sup>40</sup> See NASAA Letter at 1-3.

compliance with the proposed rule, discover best reporting practices to share with its members, perform comparisons to facilitate risk-based examination selections, and determine whether disclosures give rise to the need for investigation.<sup>41</sup> FINRA agrees and, as discussed above, is proposing to publish both the new OTC Equity Security reports and existing SEC Rule 606(a) reports in a centralized location on its website, free of charge and without usage restrictions. Finally, NASAA expressed its belief that investor education is necessary to make the reports useful, and accordingly suggested that FINRA develop and post information for investors on how to read and interpret the data. Alternatively, NASAA suggested that FINRA could develop standard educational materials that firms can either link to or be required to make available with the reports.<sup>42</sup> FINRA agrees that investor education would be useful and, as noted above, intends to engage in investor education efforts regarding the purpose, content, and potential limitations of the disclosures.<sup>43</sup>

Fidelity also supported the proposed rule change, stating that it largely accomplishes the goals of providing transparency into broker routing and economic practices in OTC Equity Securities, an asset class that has experienced significant growth but remains opaque.<sup>44</sup> Fidelity also made several recommendations to enhance the effectiveness of the proposed rule change. First, Fidelity recommended that FINRA and the SEC should consider how various order routing disclosure reports, including SEC Rules 605 and 606 reports, are used in the marketplace and could be used together, suggesting that FINRA and the SEC should coordinate their oversight of order routing reports to ensure consistency in process and interpretation.<sup>45</sup> FINRA agrees with and, as described above, has sought to align the form and content of the new OTC Equity Security reports as closely as possible with the existing Rule 606(a) reports, unless there was a

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<sup>41</sup> See supra note 40 at 3-4.

<sup>42</sup> See supra note 40 at 5.

<sup>43</sup> See supra note 23.

<sup>44</sup> See Fidelity Letter at 1-2.

<sup>45</sup> See supra note 44 at 2-3.

reason for the content to differ due to the unique characteristics of the OTC market. FINRA believes that this approach will assist in ensuring consistency in the process for generating the reports and regulatory interpretation concerning the reporting framework. FINRA also expects to continue its engagement with the SEC regarding order routing and execution quality information more broadly.

Second, Fidelity recommended that FINRA make publicly available a list of OTC Equity Securities appearing in each section of the proposed OTC Equity Security reports, and provide further clarity concerning the definition of market center and fees to be disclosed.<sup>46</sup> As noted above, FINRA will publish a list of the OTC Equity Security symbols that fall under each category to assist members in generating the reports and provide consistency across reports. FINRA has also provided clarifications regarding the scope of venues that should be disclosed on the reports and the types of fees that should be included.<sup>47</sup> FINRA will continue to engage with members to provide additional guidance on these and other issues as appropriate.

Third, Fidelity stated that FINRA should explore obtaining data for all, or part, of the proposed OTC Equity Security reports from broker-dealer CAT submissions.<sup>48</sup> FINRA continues to believe that the most efficient and comprehensive means of providing the data included in the OTC Equity Security order routing disclosures is for members to generate the reports directly.

Finally, Fidelity expressed support for FINRA to consolidate all order routing reports on a centralized website and make this content available without cost.<sup>49</sup> As discussed above, FINRA is proposing to publish both the new OTC Equity Security reports and existing SEC Rule

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<sup>46</sup> See supra note 44 at 3-4.

<sup>47</sup> See supra notes 16 and 18.

<sup>48</sup> See supra note 44 at 4-5.

<sup>49</sup> See supra note 44 at 5.

606(a) reports in a centralized location on its website, free of charge and without usage restrictions.

FIF neither supported nor opposed the proposed rule change but provided comments focused on achieving the most effective implementation in the event that FINRA moves forward with the proposed rule change. FIF first provided its views regarding the entity that should be reported as the “venue” on the reports when there are multiple levels of routing for an order, including the requirement to “look-through” to the execution venue.<sup>50</sup> FIF stated that, when a customer-facing broker-dealer routes an order to a second broker-dealer, the customer-facing broker-dealer should report on its financial arrangement with the second broker-dealer instead of the fee arrangement between the second broker-dealer and that downstream venue. FIF stated that there are many scenarios where a customer-facing broker-dealer will route an OTC Equity Security order to another broker-dealer that is neither a market maker nor an alternative trading system and therefore the order is further routed by the receiving broker-dealer. In these situations, FIF argued that the customer-facing broker-dealer should report the second broker-dealer on any reports instead of the final downstream venue. Reporting the final downstream execution venue, *i.e.*, the “look-through” requirement, would ignore any payment for order flow made by the second broker-dealer to the customer-facing broker. FIF also suggested modifying the proposed rule change such that any reference to “venue” be changed to “venue or broker” and any reference to “routed for execution” be changed to “routed” or “routed for execution or further routing” or “routed for execution (by the recipient or another party).” FIF further stated that the look-through requirement would greatly increase the cost of the report due to the costs associated with coordination between the customer-facing broker-dealer and the second broker-dealer that routes to a venue for execution.<sup>51</sup>

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<sup>50</sup> See FIF Letter at 1-3.

<sup>51</sup> See *supra* note 50 at 3.

Consistent with the requirements of SEC Rule 606(a), FINRA’s proposal would cover the venues to which non-directed held orders in OTC Equity Securities were “routed for execution.” As discussed above, the SEC has provided guidance in the SEC Rule 606(a) context that, if a broker-dealer routes orders to another broker-dealer, that receiving broker-dealer would be considered to be the relevant venue if that receiving broker-dealer executes orders. However, if the receiving broker-dealer does not execute orders, it would not be a venue to which orders were “routed for execution.” Rather, the venue to which the receiving broker-dealer subsequently routed the orders for execution (including child orders) would be the relevant venues for SEC Rule 606(a) reporting purposes. Further, while the reporting responsibility remains with the customer-facing broker-dealer, the customer-facing broker-dealer may contract with the receiving broker-dealer for assistance in meeting its reporting responsibilities.<sup>52</sup> FINRA continues to believe that this aspect of the proposed order routing disclosures for OTC Equity Securities should be consistent with the SEC Rule 606(a) disclosures for NMS Securities, including with respect to the “look-through” requirement when a receiving broker-dealer does not execute orders. FINRA believes that aligning the scope of the disclosures with the requirements of SEC Rule 606(a) would reduce the burden of the new disclosure requirements because members already have experience with SEC Rule 606(a) and may be able to utilize existing systems and arrangements with receiving broker-dealers to provide the disclosures for OTC Equity Securities. Further, because the purpose of the proposed disclosures—providing information about members’ orders routing practices and potential conflicts of interest related to execution venues—is the same as the purpose of SEC Rule 606(a) for NMS Securities, FINRA believes that the same types of venues should be covered by the new reports for OTC Equity Securities.

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<sup>52</sup> See SEC Division of Trading and Markets, Responses to Frequently Asked Questions Concerning Rule 606 of Regulation NMS, Question 12.01.



FIF also responded to a number of specific questions posed in Regulatory Notice 21-35.<sup>53</sup> As an initial matter, FIF agreed with a number of aspects of the proposed rule change, including (i) the quarterly reporting timeframe of the reports; (ii) not providing a separate reporting category for grey market securities; (iii) limiting the proposed reports to held orders in OTC Equity Securities; (iv) not breaking out the reports by market orders, marketable limit orders, non-marketable limit orders, and other orders; (v) requiring reporting of payments per order, rather than per share; (vi) not adopting customer-specific held order disclosures, like those required under SEC Rule 606(b)(3), at this time; and (vii) not adopting execution quality disclosures, like those required under SEC Rule 605, at this time.

FIF requested that FINRA incorporate a de minimis venue exception parallel to the exemptive relief that the SEC has provided with respect to the SEC Rule 606(a) reports. As noted above, FINRA agrees and has included a parallel exception in the proposed rule change.<sup>54</sup>

FIF also expressed support for centralized publication of SEC Rule 606(a) reports and, if adopted, the proposed OTC Equity Security reports on the FINRA website (or another third-party website in a manner that can be accessed by all market participants at no cost), and further recommended that the SEC, FINRA, the other self-regulatory organizations and FINRA CAT consider how current reporting systems, such as the CAT, can be leveraged to reduce the general reporting burden for firms. As discussed above, FINRA is proposing to publish both the new OTC Equity Security reports and existing SEC Rule 606(a) reports in a centralized location on its website, free of charge and without usage restrictions. However, FINRA is not proposing to use CAT data for the proposed disclosure requirements in light of restrictions on the use of CAT data and FINRA's continued belief that, as for SEC Rule 606(a) reports, the most efficient method to create and publish the required disclosures is for members to provide the routing information directly.

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<sup>53</sup> See FIF Letter at 3-9.

<sup>54</sup> See supra note 17.

FIF stated that the proposed categories of OTC Equity Securities are appropriate and recommended that FINRA publish and maintain a file of which symbols are included in each category. As noted above, FINRA will publish a list of the OTC Equity Security symbols that fall under each category to assist members in generating the reports and provide consistency across reports.

FIF stated that the proposed disclosures may have unintended consequences, as increased transparency may lead broker-dealers to change how they route held orders in OTC Equity Securities in ways that may be suboptimal for customers on execution quality dimensions that are less easily observable. To address this concern, FIF suggested that FINRA could publish guidance to investors on the purpose, content, and potential limitations of the reports. While FINRA does not believe that the transparency will likely result in suboptimal executions, FINRA intends to, as appropriate, provide members, investors, and others with information about the purpose, content, and potential limitations of the reports.

FIF further stated that the industry requires a significant time period for implementation, including sufficient time for industry members to identify and obtain guidance from FINRA on applicable interpretive questions. FINRA intends to provide an appropriate amount of time for implementation of the proposed rule change and will work with the industry to provide guidance as appropriate on interpretive questions. In particular, FIF requested that FINRA meet with industry members to discuss how the proposed routing disclosures should be applied to orders executed through OTC Link, and also requested that FINRA provide additional guidance on the level of detail required for the material aspects disclosure. FINRA intends to continue to engage with members and other interested parties prior to implementation of the proposed rule change, including to discuss order routing disclosures in scenarios involving OTC Link. FINRA also intends to provide guidance as appropriate on other interpretive questions, including the content of the material aspects disclosure. However, FINRA notes that it would generally expect the

level of detail included in the material aspects disclosures to be consistent with that provided in SEC Rule 606(a) reports for NMS Securities.

FIF generally agreed with the proposed content of the OTC Equity Security disclosure reports, but recommended removing the requirement that members report the number of directed orders because the routing decision in such cases is outside the control of the broker-dealer. FINRA notes that, as described above and consistent with SEC Rule 606(a), the proposed disclosures would apply only to non-directed held orders. The proposed reports would include aggregate statistics regarding the percentage of total orders that were held and not held orders, and the percentage of held orders that were non-directed orders, but no other information about directed orders would be required.

Finally, FIF stated that its members are divided on whether the reporting requirements should include routes to brokers and venues outside the U.S. FIF recommended that multiple approaches should be permitted and that the reporting firm should indicate which approach was adopted on the webpage accompanying the routing reports. In any case, FIF stated that, if a foreign issuer does not have F shares in the U.S., the order should not be reportable. FINRA believes that, consistent with SEC Rule 606(a), the OTC Equity Security disclosures should include information about venues where a member's orders are routed for execution, regardless of the location of such venue. Particularly where orders are non-directed, the member has discretion to choose where it routes orders for execution; therefore, permitting a member to omit foreign venues could raise arbitrage concerns and provide incomplete information to investors. Moreover, information about incentives and potential conflicts of interest is just as relevant where an execution venue is located abroad. With respect to F shares, FINRA notes that orders in any security that meets the definition of OTC Equity Security would be included in the reports regardless of the location of the issuer.

LPL did not support the proposed rule change, stating that, while LPL supports efforts to provide greater transparency as to the handling of orders, the proposed rule change would

impose a significant burden on firms without providing useful information to investors.<sup>55</sup> LPL stated that the proposed rule change would have limited benefits as compared to SEC Rule 606(a) for NMS Securities, which LPL believes can provide investors with useful information because it can be combined with order execution information available pursuant to SEC Rule 605; by contrast, the proposed OTC Equity Security disclosures would not have parallel execution quality disclosures.<sup>56</sup>

FINRA believes that the proposed order routing disclosures will provide investors and other market participants with useful information, even in the absence of Rule 605-like disclosures at this time.<sup>57</sup> FINRA believes the proposed order routing disclosures will facilitate investor understanding of where their brokers are routing orders and the relationships their brokers have with those execution venues. In addition, FINRA notes that SEC Rule 606(a) includes information about order routing practices for NMS Securities that are options, and options are not included in the execution quality disclosures under SEC Rule 605.

LPL also stated its belief that the proposed rule change would subject firms to costly burdens, including internal technology costs to identify and gather the needed data, vendor costs to prepare quarterly reports, and employee time to implement and supervise disclosures.<sup>58</sup> Given that OTC Equity Securities are a very small part of LPL's core business, LPL stated that these additional burdens may have a chilling effect and cause firms to stop accepting orders for OTC Equity Securities. As discussed above, FINRA acknowledges that members would incur costs to

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<sup>55</sup> See LPL Letter at 1.

<sup>56</sup> See supra note 55 at 1-2.

<sup>57</sup> In light of differences between the market for NMS Securities and OTC Equity Securities, including for example the absence of a centralized, SRO-disseminated national best bid and offer in the OTC market, FINRA is not proposing Rule 605-like execution quality disclosure requirements for OTC Equity Securities at this time. FINRA will continue to consider whether additional disclosures would provide useful information for investors in OTC Equity Securities.

<sup>58</sup> See LPL Letter at 2. LPL stated that it expects the initial costs to implement the proposed rule change would be similar to the cost of complying with recent amendments to SEC Rule 606.

capture the required data, generate the reports, publish the reports, and transmit the reports to FINRA for centralization publication. FINRA believes that such costs would be reduced for introducing firms that choose to rely on the guidance discussed above.<sup>59</sup> In any case, FINRA continues to believe that the costs associated with the proposal are outweighed by the benefits to investors and the market of the transparency provided by the proposed OTC Equity Security disclosures.

Finally, LPL stated that imposing the additional costs of the proposed OTC Equity Security disclosures on firms that do not receive payment for order flow would be both unfair and unproductive, and therefore requested that, if FINRA adopts the proposed rule change, the proposed rule change include an exemption for firms that do not receive payment for order flow.<sup>60</sup> FINRA notes that, while payment for order flow arrangements are an important component of the information that would be required to be disclosed under the proposed rule change, the proposed disclosures also include information about other payments and arrangements that members may have with execution venues that may influence a member's order routing decision. FINRA continues to believe that the proposed disclosures would be valuable for investors and other market participants more broadly, regardless of whether a particular member receives payment for order flow, because the proposed disclosures would provide investors with a better understanding of where their brokers are routing orders and the overall relationships their brokers have with those execution venues.

### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

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<sup>59</sup> See supra notes 10 and 25.

<sup>60</sup> See LPL Letter at 2-3.

- (A) by order approve or disapprove such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2022-031 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2022-031. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change. Persons submitting

comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available

publicly. All submissions should refer to File Number SR-FINRA-2022-031 and should be submitted on or before [INSERT DATE 21 DAYS FROM PUBLICATION IN THE FEDERAL REGISTER].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>61</sup>

**Sherry R. Haywood,**

*Assistant Secretary.*

[FR Doc. 2022-26445 Filed: 12/5/2022 8:45 am; Publication Date: 12/6/2022]

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<sup>61</sup> 17 CFR 200.30-3(a)(12).